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SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1930.

No. [redacted] 14

HANDY & HARMAN, PETITIONER,

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

WILLIAM C. BREED,
HUGH S. WILLIAMSON,
Counsel for Petitioner.

(35,631)

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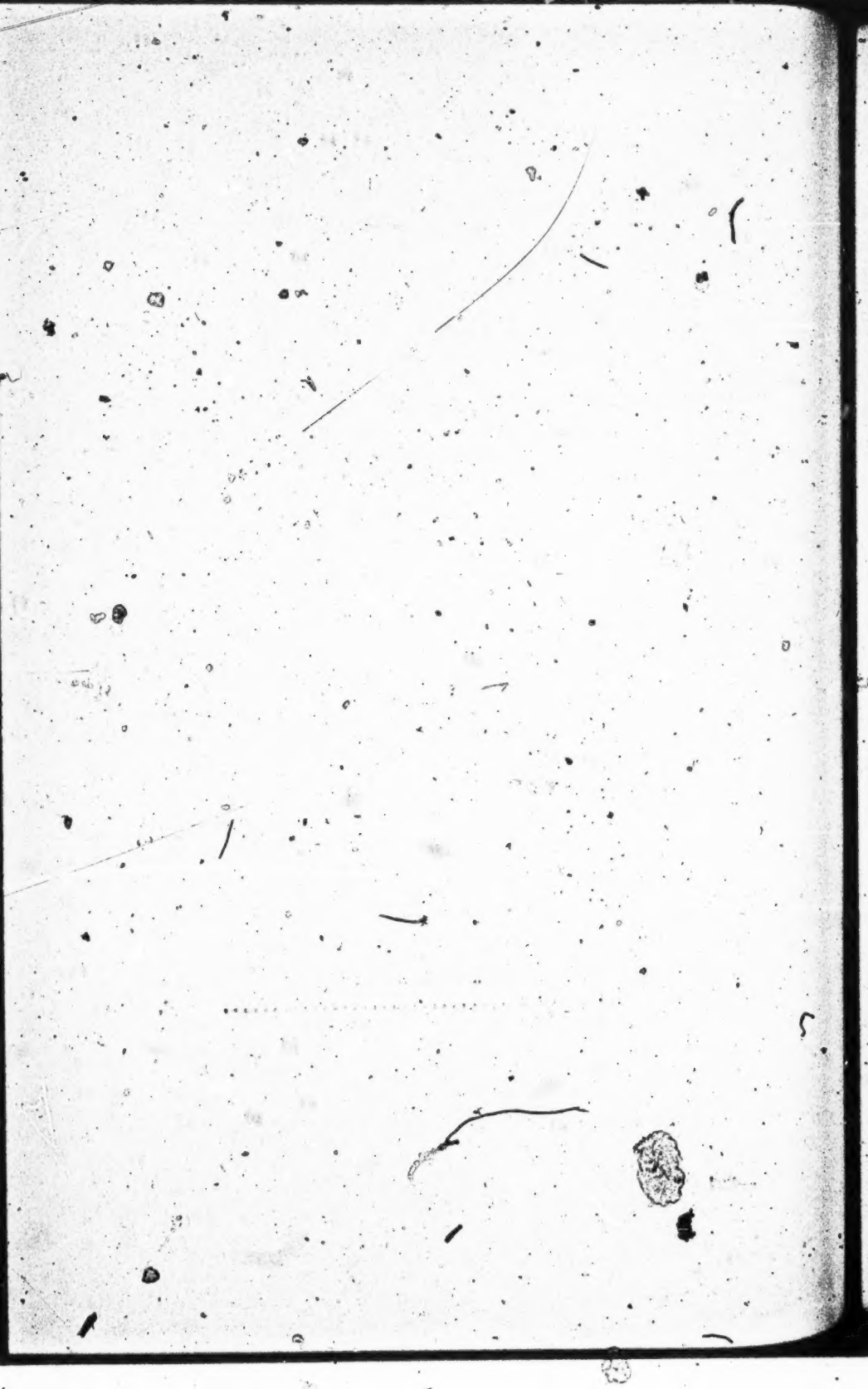

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1930.

No. 709

HANDY & HARMAN, PETITIONER,

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

PETITION.

Handy & Harman respectfully prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit entered in the above entitled case on January 12, 1931, affirming the decision of the United States Board of Tax Appeals.

Question Involved.

(*a*) In general, were Handy & Harman and Hamilton & De Loss, Inc., affiliated corporations within the meaning of Section 240 of the Revenue Act of 1918 and entitled to make consolidated returns of net income and invested capital for the period January 1, 1918, to February 1, 1919?

(*b*) Specifically, does the word "controlled" used in the statute with reference to stock mean something different from "owned" and, if so, must it be "at least a control legally enforceable" or is *actual* control sufficient?

Statement.

The petitioner, Handy & Harman, claimed the right to file consolidated returns of net income and invested capital with Hamilton & De Loss, Inc., for the year 1918 and the period January 1 to February 1, 1919, upon the ground that the two corporations were affiliated within the meaning of Section 240 of the Revenue Act of 1918.

The Commissioner of Internal Revenue denied this claim, rejected petitioner's claims for abatement for 1918 amounting to $25,800.99 and asserted a deficiency for 1919 of $3,156.90 (R. 1[illegible]). The United States Board of Tax Appeals approved the aforesaid determination of the Commissioner and held the two corporations to be not affiliated (R. 26-38). Upon petition for review the United States Circuit Court of Appeals

for the Second Circuit affirmed the decision of the Board of Tax Appeals (R. 79).

The whole controversy turns upon the question of whether or not 20 per cent of the stock of Hamilton & De Loss, Inc., originally issued to and standing in the name of Harold H. Hamilton on the books of that corporation was "controlled" within the meaning of the statute by the six men who owned practically all of the remaining stock of Hamilton & De Loss, Inc., and who also admittedly owned or controlled substantially all of the stock of Handy & Harman.

The issue arises under the subdivision of the statute providing that corporations shall be deemed affiliated "if substantially all of the stock of two or more corporations is *owned* or *controlled* by the same interests."

The decisions of the various Circuit Courts of Appeals show that two well defined and conflicting theories have been developed with respect to the meaning of the word "controlled":

(1) The Second Circuit Court of Appeals adheres to the theory that the words "owned" and "controlled" are practically synonymous and that to meet the requirements of the statute the minority stock must be controlled *through legally enforceable means.*

(2) Five of the other Circuit Courts of Appeals have placed a different construction upon the statute and hold that where the corporations are operating as a business and economic unit

actual control of the voting stock of the minority is sufficient whether or not based on legally enforceable means.

It has never been questioned that Handy & Harman and Hamilton & De Loss, Inc., were operated as a business and economic unit, and the Circuit Court of Appeals concedes that if the view be accepted that control means *actual* control of the voting power of the minority stock, whether or not legally enforceable, it can scarcely be doubted that the statutory requirements with respect to the ownership or control of stock necessary for affiliation have been met.

Statute Involved.

Revenue Act of 1918, c. 18, 40 Stat. 1067:

> SECTION 240(*a*). That corporations which are affiliated within the meaning of this section shall, under regulations to be prescribed by the Commissioner with the approval of the Secretary, make a consolidated return of net income and invested capital for the purposes of this title and title III, and the taxes thereunder shall be computed and determined upon the basis of such return: * * *
>
> (*b*) For the purpose of this section two or more domestic corporations shall be deemed to be affiliated, * * *.
>
> (2) If substantially all the stock of two or more corporations is *owned* or *controlled* by the same interests.

Reasons for Granting Petition.

A. *Conflict with Other Decisions.*

The decision of the Second Circuit Court of Appeals in this case is directly in conflict with decisions of the Circuit Courts of Appeals in the following cases:

Kile & Morgan Co. *v.* Commissioner, 41 F. (2d) 925 (C. C. A. 1);

J. Rogers Flannery *v.* Commissioner, 42 F. (2d) 11 (C. C. A. 3);

Pelican Ice Co. *v.* Commissioner, 37 F. (2d) 285 (C. C. A. 5);

Great Lakes Hotel Co. *v.* Commissioner, 30 F. (2d) 1 (C. C. A. 7);

Commissioner *v.* Richfield Oil Co., 42 F. (2d) 360 (C. C. A. 9).

The decision of the Circuit Court of Appeals in the instant case is also in conflict with the following decisions of the United States Court of Claims:

Eby Shoe Co., Inc., *v.* United States, 44 F. (2d) 273;

Ullman Manufacturing Co. *v.* United States, 67 Ct. Cls. 104.

B. *General Importance of the Questions.*

Petitioner has been informed and believes that numerous cases involving the application of the 1918 statutory provisions for consolidated returns and the similar provisions of later acts are still pending before the Bureau of Internal Revenue, the Board of Tax Appeals, and in the courts.

WHEREFORE it is respectfully submitted that this petition for a writ of certiorari to review the judgment of the Circuit Court of Appeals for the Second Circuit should be granted.

HANDY & HARMAN,
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Counsel for Petitioner.

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BRIEF IN SUPPORT OF PETITION.

Opinions Below.

The opinion of the United States Board of Tax Appeals (R. 26-38) is reported in 17 B. T. A. 980.

The opinion of the Circuit Court of Appeals has not been reported, but appears in the Record, pages 75-79.

Jurisdiction.

The judgment of the Circuit Court of Appeals sought to be reviewed was entered January 12, 1931. Jurisdiction to issue the writ is found in the provisions of Section 240(*a*) of the Judicial Code as amended by the Act of February 13, 1925.

Statute Involved.

The material portions of Section 240 of the Revenue Act of 1918 are set forth in the petition for certiorari.

The Facts.

There is no dispute as to the facts in the instant case and in substance they are as follows:

Handy & Harman is a New York corporation with its principal office in New York City and is engaged in dealing in gold and silver bullion (R. 27). In 1916 Hamilton & De Loss, Inc., a Connecticut corporation, was caused to be organized by the officers and ma-

jority shareholders of Handy & Harman to take over a department of the latter's silversmithing business (R. 28, 29). At all times during the taxable periods involved six men, Messrs. Parker W. Handy, John L. Harman, Harry H. De Loss, William B. Sewell, George C. Gerrish and Robert H. Leach owned outright 93.71 per cent of the capital stock of Handy & Harman, the remaining shares being owned by employees and most of said shares being held subject to the corporation's option to repurchase should the shareholders leave its employ. The same six men also owned 76.66 per cent of the stock of Hamilton & De Loss, Inc., while 20 per cent of the stock of this corporation stood in the name of Harold H. Hamilton, who was not a stockholder in Handy & Harman (R. 29, 30).

At the time f the organization of Hamilton & De Loss, Inc., Hamilton, a man of large experience in silversmithing, had been invited to become president of the new corporation (R. 28). Hamilton, however, had no money to purchase stock in the new corporation and the purchase price of the 20 per cent interest standing in his name was financed through arrangements made by De Loss whereby Hamilton borrowed the necessary money from a bank upon his notes endorsed by De Loss (R. 30). Prior to the beginning of the taxable periods here in question Hamilton executed an "irrevocable stock power" assigning his stock in Hamilton & De Loss, Inc., to one Robert M. Higgins (R. 64, 65), who subsequently executed a similar instrument assigning the stock to De Loss (R. 62, 63), who deposited it with the bank as collateral security

for the notes. Hamilton never paid anything upon the notes. In 1919 he became insolvent and on February 1, 1919, De Loss paid the notes and took over the stock (R. 30). Prior to the last-mentioned date Hamilton attended all stockholders' meetings of Hamilton & De Loss, Inc., but never voted in opposition to the men who owned the majority stock of both corporations. Hamilton received a salary from Hamilton & De Loss, Inc., but its other officers and directors were also officers or employees of Handy & Harman and received their compensation solely from the latter corporation, even though all or a large part of their working hours were devoted to the former (R. 30, 31).

The plants of both corporations here involved were located in Bridgeport, Connecticut, within 150 yards of each other, and the two corporations were operated as a business and economic unit. In 1918 Hamilton & De Loss, Inc., entered into a contract with the United States Government for the making of eye pieces for gas masks. While this contract was taken in the name of Hamilton & De Loss, Inc., the petitioner financed the contract, melted and rolled the metal and furnished it to Hamilton & De Loss, Inc., which stamped out the eye pieces and returned it to the petitioner for remelting. The entire contract was performed in that manner, neither plant being equipped to do the work independently of the other. Neither the petitioner nor Hamilton & De Loss, Inc., made any profit from the eye-piece contract. Hamilton & De Loss, Inc., sustained a net loss in the year 1918 and during the month of January, 1919 (R. 30-33).

Specifications of Error.

The Circuit Court of Appeals erred in holding:

(1) That the control of stock referred to in the statute must be based on legally enforceable means.

(2) That Handy & Harman and Hamilton & De Loss, Inc., were not affiliated corporations and not entitled to make consolidated returns of net income and invested capital.

ARGUMENT.

I.

The question presented by the instant case is to what extent, if any, the word "controlled" is broader than the word "owned" and arises under the subdivision of the statute providing that corporations shall be deemed affiliated "if substantially all of the stock of two or more corporations is *owned* or *controlled* by the same interests."

The Second Circuit Court of Appeals has adopted a narrow construction of the statute and holds that if control means something different from ownership "it must at least be a control legally enforceable." Under this construction the word "control" becomes practically synonymous with the word "ownership".

Other Circuit Courts of Appeals have placed a different construction upon the statute and have held that when the corporations are operating as a business unit *actual* control of the voting power of the minority stock

is sufficient whether or not based upon legally enforceable means. This conflict between the Circuit Courts of Appeals is clearly recognized and definitely set out in the opinion of the Second Circuit Court of Appeals in the instant case, as follows:

> "In United States *v.* Cleveland P. & E. R. Co., 42 F. (2d) 413 (C. C. A. 6), Judge Mack thoroughly reviewed the legislative history of the statute in question and the judicial decisions which have construed it.
>
> His opinion demonstrates that the courts are not in accord as to the meaning to be given to the word 'control' in determining whether or not affiliation exists. One line of cases holds that when the corporations are operating as a business unit, actual control of the voting power of the minority stock is sufficient, though based on revocable proxies, relationships of blood or friendship, or perhaps even mere acquiescence of the minority. To the authorities cited by Judge Mack as upholding this view may be added the later cases of Kile & Morgan Co. *v.* Commissioner, 41 F. (2d) 925 (C. C. A. 1); J. Rogers Flannery & Co. *v.* Commissioner, 42 F. (2d) 11 (C. C. A. 3); Commissioner *v.* Richfield Oil Co., 42 F. (2d) 360 (C. C. A. 9); Eby Shoe Co., Inc., *v.* United States, 44 F. (2d) 273 (Ct. Cl.). If this view be accepted it can scarcely be doubted that Hamilton's stock was 'controlled' by De Loss and his associates.
>
> The other line of cases adopts a narrower interpretation, and holds that if 'control' means something different from ownership of stock, it must at least be a control legally enforceable. See authorities cited in United States *v.* Cleve-

land P. & E. R. Co., *supra*. *This court is already committed to the narrower view, Commissioner v. Adolph Hirsch & Co., supra; and we are disposed to adhere to it until an authoritative voice declares it wrong.*" (Italics ours.)

The conflict between the Circuit Courts of Appeals with respect to the meaning of the word "controlled" is recognized and stated in *United States* v. *Cleveland, Painesville & Eastern Railroad Co., Inc.*, 42 F. (2d) 413, 417 (C. C. A. 6):

> "(*a*) Some five cases may be disregarded since the facts clearly revealed either complete legal ownership of voting stock, or complete lack of ownership and/or control. The remaining decisions fall roughly into two classes, those holding that ownership and control are practically synonymous and that affiliation can exist only where substantially the entire beneficial interest in the stock is in the hands of the same individuals or corporations, or one corporation owns substantially all the stock of another, and those holding that actual control of an economic business unit, obtained through stock control based on acquiescense, blood relation, or proxy, is sufficient."

The Second Circuit Court of Appeals recognizes that if the broader interpretation of the statute be accepted "it can scarcely be doubted that Hamilton's stock was 'controlled' by De Loss and his associates." In other words, under the decision in the instant case denying to petitioner the right to file consolidated returns of net income and invested capital with Hamilton & De

Loss, Inc., petitioner is compelled to pay substantially larger taxes than other taxpayers similarly situated but located in any of said other five circuits.

II.

Numerous cases involving the application of the 1918 statutory provisions for consolidated returns are still pending before the Bureau of Internal Revenue, the Board of Tax Appeals, and the various Federal courts. The Revenue Acts of 1921, 1924 and 1926 contain consolidated returns' provisions under which questions almost identical with that of the instant case have arisen.

In *United States* v. *Cleveland, Painesville & Eastern Railroad Co., Inc., supra,* Judge Mack, at page 414, said the following with respect to the importance of the question here presented:

> "(1) Few provisions in any of the income tax statutes enacted since the ratification of the Sixteenth Amendment have required a greater amount of litigation and judicial labor for their clarification than those relating to 'invested capital' * * * and those attempting to define 'corporate affiliation' in the Act of 1918 and later statutes."

No decision has been rendered by this Court upon the subject here involved, and it is respectfully submitted that the petition for a writ of certiorari to review the judgment of the Circuit Court of Appeals for the Second Circuit should be granted in order that the

conflict among the decisions of the Circuit Courts of Appeals be settled and a final rule be established for the guidance of taxpayers, the courts and the Treasury Department.

Respectfully submitted,

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